IN THE UNITED STATES BANKRUPTCY COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

In re:	)	
	)	
JEFFERSON COUNTY,	)	CASE NO. 11-05736-TBB9
ALABAMA,	)	Chapter 9
	)	
Debtor.	)	

EMERGENCY MOTION OF THE JEFFERSON COUNTY SEWER SYSTEM RECEIVER FOR (A) A DETERMINATION THAT THE RECEIVER SHALL CONTINUE TO OPERATE AND ADMINISTER THE SEWER SYSTEM PURSUANT TO THE RECEIVER ORDER OR (B) FOR RELIEF FROM AUTOMATIC STAY OR OTHER APPROPRIATE RELIEF

John S. Young, Jr., LLC (the "Receiver") as a party-in-interest,[1] by and through its undersigned counsel, moves this Court pursuant to 11 U.S.C. §§ 362(d), 903, 904, 922(b) and (d), and 928, and Fed. R. Bankr. P. 4001(a) and 9014, for a determination that the Receiver (i) may continue operating the Jefferson County Sewer System (the "System"), (ii) is not required to turn over control of the System, and (iii) retains its authority under the order appointing the Receiver, including the authority to fix and charge rates pursuant to the order appointing the Receiver (the "Receiver Order"), or alternatively, for relief from the automatic stay such as terminating, annulling, modifying or otherwise conditioning the stay, so that the Receiver may (i) continue in possession and control of the System, (ii) take any and all action necessary to preserve, protect, administer and operate the System, including any action to fix and charge rates for the System, and (iii) collect and pay the revenues from the System, less operating expenses, to the creditors whose claims are secured by such revenues pursuant to the order Receiver Order.

[1] The Receiver is a party in interest as a result of its possession and control of property that may belong to the Debtor and its appointment by Court Order to administer property of the Debtor, pay claims against the Debtor and manage the financial interests related to the operation of the Sewer System.

By separate motion, the Receiver has also requested that this Motion be heard on an expedited basis. In support of this Motion, the Receiver states as follows:

I. Introduction

The Receiver files this Motion requesting that the Court affirm that the Receiver has full authority to continue in possession, operation and control of the System pursuant to the terms of the Receiver Order and under the supervision of the State Court. The Receiver is required to file this Motion because, by letter sent the same day as the filing of the petition, the Debtor demanded that the Receiver turn over the System to the Debtor by close of business on November 10, 2011; however, as fully explained in this Motion, the Debtor cannot require the Receiver to return possession and control of the System to it.

In large part in response to the corruption and mismanagement of the System, as well as in response to the Debtor's refusal to properly administer rate increases necessary to operate the System and service the System's debt, the Circuit Court of Jefferson County appointed the Receiver over one year ago pursuant to the Receiver Order. The Debtor never appealed the Receiver Order. The Receiver, under the supervision of the Jefferson County Circuit Court, a part of the judicial branch of the State of Alabama, has operated the System ever since in accordance with the powers and duties spelled out in the Receiver Order.

The Court lacks the statutory authority to remove the Receiver or otherwise limit the Receiver's control of the System. Although Section 543 of the Bankruptcy Code generally requires a receiver to turn over property of a debtor upon the filing of the petition for relief, Section 543 is inapplicable to Chapter 9 cases. Therefore, there is no statutory authority for the Court to remove the Receiver or modify its powers. Congress's omission of Section 543 was intentional and resulted from Congress's concerns over the intersection between Chapter 9 and

the Tenth Amendment; these concerns are further embodied in the limitations of the Court's powers in Section 903, which also prevents interference with the Receiver's control of the System as an officer of a state court exercising control over a subdivision of the Debtor. Likewise, the Bankruptcy Code does not allow the Court to interfere with the Receiver's rate-making authority because doing so would countermand state law and Section 904's limitations on the Court's authority over the Receiver, which has stepped into the shoes of the Debtor for purposes of operating the System.

Moreover, the Court should abstain from disturbing the status quo in reliance on: (i) the Rooker-Feldman Doctrine's prohibition against federal court review of final state court decisions, (ii) mandatory abstention under 28 U.S.C. § 1334(c)(2), (iii) permissive abstention under 28 U.S.C. § 1334(c)(1); and (iv) the Johnson Act and other federal precedent on judicial interference in utility rate-making processes.

Finally, even if the Court finds that it does have the authority to remove the Receiver or limit the Receiver's ratemaking authority or that the Court should not abstain from exercising jurisdiction over the Receiver, the Court should nonetheless grant the Receiver relief from the automatic stay to continue its duties under the Receiver Order because of the Debtor's inability to properly manage the System.

II. Procedural Posture and Jurisdiction

1. On November 9, 2011 (the "Petition Date"), Jefferson County, Alabama (the "County" or the "Debtor"), filed a voluntary petition for relief under Chapter 9 of Title 11 of the United States Code, § 101, *et seq*. (the "Bankruptcy Code").

2. The Receiver brings this motion (the "Motion") under Sections 362(d) and 922(b) and (d) of the Bankruptcy Code and Bankruptcy Rules 4001(a)(1) and 9014. As the custodian of the System, the Receiver is a party-in-interest in this case.

3. The Court has jurisdiction to determine whether the automatic stay of Sections 362(d) and 922(a) of the Bankruptcy Code applies to the Receiver pursuant to 28 U.S.C. § 1334(b). Likewise, determination of whether the stay applies is a core proceeding under 11 U.S.C. § 157(b)(2), but as further explained below, this Court should abstain from exercising jurisdiction over the System or its assets.

4. Venue of this matter is proper in this Court pursuant to 28 U.S.C. §§1408 and 1409(a).

III. Facts

A. The Debtor's Defaults and the Appointment of the Receiver

5. The Bank of New York Mellon, in its capacity as Indenture Trustee (the "Indenture Trustee") filed suit against the Debtor in September 2008 with the United States District Court for the Northern District of Alabama, styled *The Bank of New York Mellon v. Jefferson County, Alabama, et al.*, No. CV-08-P-1703-S for various defaults under that certain Indenture dated as of February 1, 1997, and the supplements thereto (the "Indenture"). After reviewing reports of the Special Masters, including John S. Young, the current Receiver, in an opinion entered on June 12, 2009, Judge Proctor found that there was ample evidence of "fraudulent conduct and suppression by the County" as well as waste and improper accounting. Despite finding that the Indenture Trustee was entitled to the appointment of a receiver, the Court found that the Johnson Act (28 U.S.C. § 1342) precluded a federal court from appointing a receiver with authority to fix and charge sewer rates.

6. The Trustee then filed an action in the Circuit Court of Jefferson County, Alabama (the "State Court") styled *The Bank of New York Mellon, as Indenture Trustee v. Jefferson County, Alabama, et al.*, Case No. CV-2009-02318 (the "Receivership Case") on August 3, 2009 seeking the appointment of a receiver. On September 22, 2010, the State Court entered a final order (the "Receiver Order") granting the motion for partial summary judgment of the Indenture Trustee. A true and correct copy of the filed Receiver Order is attached hereto as **Exhibit A**. The Debtor did not appeal the Receiver Order.

7. In the Receiver Order, the State Court found that the Debtor had defaulted on its obligations owed to the Indenture Trustee and the holders of the warrants issued pursuant to the Indenture, and awarded a money judgment against the Debtor in the amount of $515,942,500.11. *See* Exhibit A, at pp. 2-4, 22, ¶¶ 4-12, 30. A true and correct copy of the Indenture is attached hereto as **Exhibit B**.

8. Specifically, the State Court found that the Debtor had defaulted by, among other things,

(a) Failing to pay principal and interest then due under the Indenture, *see* Exhibit A, at pp. 2-3, ¶¶ 4-5;

(b) Failing to set rates and charges for sewer service sufficient to pay the indebtedness of the System as required by Sections 12.5(a), (b) and (c) of the Indenture, *see* Exhibit A, at pp. 3-4, ¶¶ 6-7, 12;

(c) Failing to deposit System revenues into the System's Revenue Account as required by Section 11.1 of the Indenture, *see* Exhibit A, at p. 3, ¶ 8; and

(d) Failing to maintain separate books and records for the System and failing to provide financial statements to the Indenture Trustee as required by the terms of the Indenture, *see* Exhibit A, at p. 4, ¶ 11.

9. The State Court held that Section 13.2(c) of the Indenture, which provides for the appointment of a receiver to administer and operate the System with power to fix and charge rates and collect revenues, is valid and enforceable under Alabama law, and that the Debtor and its taxpayers and citizens are precluded from challenging the validity of the covenants in and provisions of the Indenture pursuant to the validation order of the Jefferson County Circuit Court entered August 24, 2001. *See* Exhibit A, at p. 5, ¶ 15.

10. The State Court found that the Trustee had met all requirements for the appointment of a receiver as set out in the Indenture, Alabama Code Section 6-6-620, and the controlling legal standards in the State of Alabama. *See* Exhibit A, at p.7, ¶ 20.

11. Pursuant to the Receiver Order, the State Court appointed the Receiver to take exclusive possession and control over the System and its assets, accounts and revenues, to administer and operate the System, to fix and charge rates, and to collect the revenues of the System and, after payment of the expenses of maintaining and operating the System, apply the revenues in accordance with the Indenture and applicable state law, all to the exclusion of the Debtor or any other person. *See* Exhibit A, at pp. 8-15, 17, ¶¶ 2-5, 10.

12. The State Court also granted the Receiver the sole and exclusive right and authority to do the following:

a. File, institute, prosecute, defend, or intervene in any action or proceeding before any appropriate court that the Receiver, in its sole business judgment,

may deem necessary for the administration or operation of the System, *see* Exhibit A, at p. 10, ¶ 2g;

b. Hire, discharge, manage and control System Staff, *see* Exhibit A, at p. 11, ¶ 2.j; and, among other things,

c. Request from the Trustee disbursements of funds of the System then on deposit with the Trustee and available under the Indenture for capital expenditures for use by the Receiver for preservation or enhancement of the System, *see* Exhibit A, at p. 13, ¶ 2.p.;

13. The Receiver Order further provided that any claim brought against the Receiver must be filed in the State Court, and granted the Receiver the same judicial immunity as the State Court possesses. Exhibit A, at pp. 20-21, ¶¶ 20-21. Also, the Receiver Order provides that the Receiver may only be removed by order of the State Court upon appropriate motion, notice and hearing, after a showing, by clear and convincing evidence, of good cause by the Debtor or the Trustee. Exhibit A, at p. 21, ¶ 24.

14. In deciding to appoint the Receiver, the State Court determined that the Debtor's defaults under the terms of the Indenture had resulted in and would continue to result in irreparable harm to the warrant-holders because "the County has failed to abide by the terms of the Indenture and has failed to operate the Sewer System in an economical, efficient and proper manner; and the public interest and the ends of justice will be best served by the appointment of a receiver." *See* Exhibit A, at p. 6, ¶ 17.

15. The State Court further held: "Unless a receiver is appointed, the failure of the Defendants to operate the System to generate revenues sufficient to provide for the payment of the Parity Securities and other obligations outstanding against the System, and for the payment

of expenses of operating and maintaining the System *will reduce the overall value of the Trustee's collateral and result in further irreparable harm to the Trustee and the Parity Security Holders*." *See* Exhibit A, at p. 6, ¶ 19 (emphasis added).

16. The State Court additionally held that the Debtor was "specifically enjoined from taking any action, other than in this Court or by appeal of this Order, which would interfere with the Receiver's administering and operating of the System or the Assets or remove any of the Assets from the control of the Receiver." *See* Exhibit A, at p. 18, ¶ 14.

B. The Receiver's Operation of the System

17. The Receiver's mandate is "to operate and administer the System in an economical and efficient manner in compliance with the terms and conditions of the Indenture to the extent possible, and subject to applicable state and federal law." *See* Exhibit A, at p. 8, ¶ 1.

18. To that end, on June 14, 2011, the Receiver filed with the State Court the Receiver's First Interim Report on Finances, Operations, and Rates of the Jefferson County Sewer System (the "Interim Report"). A true and correct copy of the Interim Report is attached hereto as **Exhibit C**.

19. As described in the Interim Report, the Receiver has determined that the System has been underfunded and poorly managed since its inception. *See* Exhibit C, at p. 5. The Debtor's governing body, the County Commission, has refused to raise sewer rates since 2008 and has ignored all advice from outside consultants that the System was underfunded and required rate increases. *See* Exhibit C, at pp. 24-28. The Debtor has never disputed any of the findings of the Receiver in the Interim Report.

20. The Receiver has, since appointment, taken numerous actions to stabilize the System's finances, including creating the first ever comprehensive business plan for the System,

implementing a new personnel plan for the System, conducting the first ever audit of billing and collections practices, and implementing other cost-saving measures involving vehicle procurement, utility expenses, maintenance management, and accounting practices. *See* Exhibit C, at pp. 30-38. The Receiver has also formulated a capital improvement plan for the System. *See* Exhibit C, at pp. 38-40. The Receiver has also recommended a 25% rate increase for the System and intends to hold public hearings and eventually implement the increase. *See* Exhibit C, at pp. 55-74. Finally, the Receiver is exploring additional sources of revenue for the System that may be implemented in the future. *See* Exhibit C, at pp. 74-79.

21. Due to the Debtor's refusal to surrender control of the System's deposit accounts to the Receiver, despite clear and unequivocal provisions of the Receiver Order, the Receiver was required to obtain a further order from the State Court compelling the Debtor to turn over control of the System's deposit accounts to the Receiver (the "Account Control Order"). The State Court entered the Account Control Order on July 8, 2011. A true and correct copy of the Account Control Order is attached hereto as **Exhibit D**.

C. Settlement Discussions between the Debtor, the Receiver and the System's Creditors

22. After the publication of the Interim Report with its recommended 25% rate increase, the Receiver attempted to mediate a settlement among the Debtor, the Receiver and the System's creditors.

23. On September 14, 2011, the Debtor approved by resolution a term sheet with the Receiver that set a framework for negotiating definitive settlement agreements among the Debtor, the Receiver, and certain participating creditors.

24. On November 9, 2011, the Receiver presented to the County a near-final version of the definitive Agreement between the Receiver and the County. The Receiver also

participated in the drafting of definitive tender agreements to be executed by the Receiver, the Debtor and the participating creditors.

25. However, on November 9, 2011, the County rejected the Agreement presented by the Receiver and approved filing this case. On the same day, counsel for the County sent a letter to counsel for the Receiver demanding that the Receiver turnover possession and control of the System to the County. A true and correct copy of this letter is attached hereto as **Exhibit E**.

D. The Extent and Nature of the Indenture Trustee's Lien

26. Section 2.1 of the Indenture provides that the Debtor granted the Indenture Trustee an interest in and lien on the System's revenues, less operating expenses, all moneys required to be deposited in the Debt Service Fund and Reserve Fund defined in the Indenture together with any investments and reinvestments of such moneys and the income and proceeds thereof, and all moneys, rights and properties from time to time granted to the Indenture Trustee or any party as additional security for the indebtedness under the Indenture. *See* Exhibit B, at pp. 13-14, § 2.1.

27. Per Section 2.2 of the Indenture, the Indenture and the warrants issued pursuant to it are not general obligations of the Debtor. *See* Exhibit B, at p. 15, § 2.2. Accordingly, the warrant-holders can only look to the System's revenues and the funds deposited in the System's deposit accounts for payment as opposed to the full faith and credit of the Debtor.

28. In the Receiver Order, the State Court found that the Trustee has a first priority lien on, among other things, the System's revenues that remain after payment of the System's operating expenses, all funds of the System in the Indenture Trustee's possession, and all monies that the Indenture requires to be placed in the Debt Service Fund and the Reserve Fund. *See* Exhibit A, at p. 4-5, ¶ 13.

IV. Law and Argument

A. The Court Lacks the Statutory Authority to Require the Receiver to Relinquish Control of the System

1. Section 901 of the Bankruptcy Code Removes the Court's Authority to Require the Receiver to Turn Over Property of the Debtor in the Receiver's Possession and Control

Section 543 of the Bankruptcy Code provides that "[a] custodian shall…deliver to the trustee any property of the debtor held by or transferred to such custodian." Bankruptcy Code § 543(b). The Receiver is a "custodian" according to Bankruptcy Code Section 101(11) because the Receiver is a receiver appointed in a state court proceeding over property of the Debtor and was appointed to take control of such property pursuant to a contract and applicable law. *See* 11 U.S.C. § 101(11)(A) and (C). Since the Receiver was appointed over one year ago and has been in exclusive possession and operational control of the System since then, in a case other than a case under Chapter 9, the only mechanism in the Bankruptcy Code to require the Receiver to relinquish possession of the System is Bankruptcy Code Section 543.

However, Congress specifically omitted Section 543 from Bankruptcy Code Section 901, which makes certain sections (and those sections only) of the Bankruptcy Code applicable to Chapter 9 cases. Bankruptcy Code section 103(f) states, "Except as provided in section 901 of this title, only chapters 1 and 9 of this title apply in a case under such Chapter 9." 11 U.S.C. § 103(f). Section 901 does not incorporate Section 543 into Chapter 9.

Though it does not appear that any court has considered the application of Section 543 in light of its omission from Section 901(a), several courts have addressed omissions of other sections of the Bankruptcy Code from Section 901; the vast majority of them have determined that the clear mandate of Section 103(f) prevents application of sections of the Code to Chapter 9 cases where Congress has not included those sections in Section 901. *See, e.g.*, *In re East*

Shoshone Hosp. Dist., 226 B.R. 430 (Banrk. D. Idaho 1998) (Section 327 is not incorporated into Chapter 9; therefore, court could not approve debtor's counsel under Section 327); *In re County of Orange*, 179 B.R. 195 (Bankr. C.D. Cal. 1995) (Section 331 regarding interim compensation of professionals does not apply in Chapter 9); *In re Sanitary & Improvement Distr. No. 7 of Lancaster Co., Neb.*, 96 B.R. 966 (Bankr. D. Neb. 1989) (same re Sections 327-331). Treatises affirm that Chapter 9 debtors lack the authority to compel turnover of property of the debtor in the hands of third parties. *See* 5 Hon. William L. Norton, Jr. & William L. Norton III, *Norton Bankruptcy Law & Practice* § 90:15 (3d ed. 2011) (stating that Chapter 9 debtor lacks the ability to compel turnover of property seized pre-petition); *see also* 6 Alan N. Resnick & Henry J. Sommer, *Collier on Bankruptcy* ¶ 901.04 (15th ed. rev. 2011) (Sections in 901(a) "were carefully selected as those necessary or desirable to the conduct of a Chapter 9 case").

The Eleventh Circuit and Supreme Court have both provided guidance to bankruptcy courts in interpreting the Code:

> [A]s long as the statutory scheme is coherent and consistent, there generally is no need for a court to inquire beyond the plain language of the statute. . . . *The plain meaning of legislation should be conclusive, except in the rare cases in which the literal application of a statute will produce a result demonstrably at odds with the intention of its drafters.*

In re Jove Engineering, Inc., 92 F. 3d 1539, 1550 (11th Cir. 1996) (emphasis in original) (quoting *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 240-42 (1989)). Here, the language of the Bankruptcy Code leaves absolutely no doubt – a section from any chapter other than Chapters 1 or 9 that is not expressly incorporated into Chapter 9 by Section 901 does not apply in a Chapter 9 case. Section 543 does not appear in Section 901; thus, it does not apply in this Chapter 9 case. Therefore, this Court cannot require the Receiver to turn the System over to the Debtor.

Even though the language in each of Sections 103(f) and 901 is clear and unambiguous such that the Court should not have to look to their legislative history to interpret them, the legislative history nevertheless affirms that Congress purposefully excluded certain Code provisions from Section 901 to prevent bankruptcy courts from wielding unconstitutional authority over a municipal debtor's property. *See* H.R. Rep. No. 95-595, at 394, *as reprinted in* 1978 U.S.C.C.A.N. 5963, 6349-50.[2] Reading sections of the Bankruptcy Code back into Chapter 9 violates Congress's intent to deprive bankruptcy courts of *in rem* jurisdiction over a Chapter 9 debtor's property and results in an unconstitutional interference with state sovereignty. *See* 6 Alan N. Resnick & Henry J. Sommer, *Collier on Bankruptcy* ¶ 901.04 (15th ed. rev. 2011) ("Congress made scrupulous efforts to avoid the application of any section that might permit interference with the political or governmental affairs or powers of the debtor in a municipal debt adjustment case[.]").

Thus, both the clear language of Sections 103 and 901 and the statutory history of these sections are clear – no statutory mechanism exists to require the Receiver to turn over the System to the Debtor. Likewise, the automatic stay cannot apply to the System, which has already been transferred to the Receiver's control pre-bankruptcy.[3] *See also In re City of Wellston*, 42 B.R. 282 (Bankr. E.D. Mo. 1984) (holding that automatic stay did not apply to require turnover of funds garnished from Chapter 9 debtor's bank account; only mechanism for requiring turnover of those funds was a Section 547 preference action). Accordingly, the Court should enter an order

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[2] H.R. Rep. No. 95-595 states, "Section 901 makes applicable appropriate provisions of other chapters of proposed Title 11. The general rule set out in Section 103(e) is that only the provisions of chapters 1 and 9 apply in a Chapter 9 case. Section 901 is the exception, and specifies other provisions that do apply." H.R. Rep. No. 95-595, at 394. Section 103 was amended by Pub. L. No. 106-554, whereby Section 103(e) was re-lettered Section 103(f).

[3] The cases cited by the Debtor in its Demand Letter to support the Debtor's demand to turn over the System are inapplicable in this case. All of them rely on the explicit or implicit application of Sections 542 or 543; however, neither of these provisions are applicable in Chapter 9 cases.

confirming that the Receiver is entitled to retain control of the System despite the Debtor's bankruptcy.

2. The Tenth Amendment and Section 903 Limit the Court's Involvement in the State's Control of the County Through the Court-Appointed Receiver with the Result that the Debtor Cannot Use the Automatic Stay to Remove the Receiver

In *Ashton v. Cameron County Water Improvement District*, 298 U.S. 513 (1936), the United States Supreme Court struck down a statutory precursor to Chapter 9 on grounds that it violated principles of state sovereignty found in the Tenth Amendment. Subsequently, Title 11's provisions dealing with municipal bankruptcies have been modified on numerous occasions to deal with these sovereignty issues. These limitations on bankruptcy courts' authority written into Chapter 9 reflect Congress's reaction to the Tenth Amendment issues raised by the Supreme Court in *Ashton*. One of these limitations – making only a select number of Bankruptcy Code provisions available in Chapter 9 cases, is discussed above. A second limitation is found in Section 903.

Section 903 of the Bankruptcy Code provides that Chapter 9 "does not limit or impair the power of a State to control, by legislation or otherwise, a municipality of or in such State in the exercise of the political or governmental powers of such municipality, including expenditures for such exercise." 11 U.S.C. § 903. Because nothing in Chapter 9 may be interpreted to interfere with a State's power to control its municipalities, it necessarily follows that a Chapter 9 Debtor must follow state laws except where specifically preempted by federal law. *In re New York City Off-Track Betting Corp.*, 434 B.R. 131, 144 (Bankr. S.D.N.Y. 2010). The appointment of the Receiver pursuant to the provisions of the Alabama Code and order of the Jefferson County Circuit Court are efforts by the State to "control" the municipality.

The legislative history of Chapter 9 generally and Section 903 in particular demonstrates the limited scope of the Court's powers under Chapter 9:

> Thus, the powers of the court are subject to a strict limitation—that no order or decree may in any way interfere with the political or governmental powers of the petitioner, the property or revenue of the petitioner, or any income producing property. The purpose of this limitation derives from *Ashton v. Cameron Water Improvement District No. 1*, which held the first municipal bankruptcy act unconstitutional on the basis of infringement of state sovereignty. This limitation was included in the second act, and was relied upon in *Bekins v. United States* which upheld the second municipal adjustments statute.

H.R. Rep. No. 95-595, at 263 (1977), *as reprinted in* 1978 U.S.C.C.A.N. 5963, 6221. The legislative history makes it clear that bankruptcy courts may not in any way "interfere with the political or governmental powers of the petitioner, the property or revenue of the petitioner, or any income producing property." *Id.* Thus, in crafting Chapter 9, Congress made abundantly clear that violations of the jurisdictional limitations of Chapter 9, including Section 903, would result in an unconstitutional violation of State sovereignty under the Tenth Amendment. Here, any order or decree by the Court interfering with the Receiver's authority over the System and its revenues—which authority was determined under state law by final orders of the State Court—would be "interfering with" the powers, property, or revenues of the governmental entity and the right of the State, through its courts, to control its municipality.

The case *In re Richmond Unified School District*, 133 B.R. 221, 224 (Bankr. N. D. Cal. 1991), involved the appointment of an "Administrator" by the State to manage the operations of the Debtor school district. After the school district filed for bankruptcy protection, the State entered into an agreement with the school district that essentially provided that the State would lend the District funds, provided the District allowed the Superintendent to take control of the district, including the appointment of an Administrator. The Administrator then moved to

dismiss the bankruptcy case. The Court, in approving the motion to dismiss and responding to a challenge to the Administrator's authority, stated that the Administrator "will retain control of the District, whether or not the Court dismisses the case, because…the court may not interfere with the District's management." *Id*. at 226.

The Debtor stated in its Demand Letter (see Exhibit D, at p. 2) that the automatic stay applies to require the Receiver to return possession and control of the System to the Debtor, relying in particular on Section 362(a)(3). The automatic stay, however, cannot apply if it will conflict with Section 903. The State of Alabama has created, by legislation and otherwise, a legal and regulatory system that governs municipal sewer systems, the indebtedness they secure, and the remedies of creditors of those systems. These exercises of the State's sovereign power led to the appointment of the Receiver, and include: (1) statutory provisions and judicial determinations regarding the control and operation of the System, (2) statutory provisions and judicial determinations regarding the power to set sewer rates, (3) statutory provisions and judicial determinations regarding the appointment of the Receiver. *See* Ala. Code § 6-6-620 (governing appointment of receivers); Ala. Code § 11-81-180 (providing for appointment of receiver over systems including sewer system);[4] *Bankhead v. Town of Sulligent*, 155 So. 869 (Ala. 1934) (providing that appointment of a receiver ensures that statutory lien is not "a meaningless expression"); *Carter v. State ex rel. Bullock County*, 393 So. 2d 1368, 1371 (Ala. 1981) (Court did not err in appointing receiver over county tax assessor where tax assessor's refusal to perform his duties materially hampered legitimate and essential governmental functions of county); *Ex parte Davis*, 162 So. 306, 308 (Ala. 1935) (receiver is officer of

[4] This code provision specifically governs analogous bond issuances pursuant to Ala. Code § 11-81-160 *et seq.* The warrants secured by the System revenues were issued under a similar chapter, Ala. Code § 11-28-1 *et seq.*

appointing court, and appointing court should be allowed first opportunity to control litigation related to its receiver).

Moreover, the State Court vested the Receiver with the exclusive possession and control of the System and the sole and exclusive authority to fix and charge rates for the System; accordingly, the Receiver now stands in the shoes of the County as the sole rate-maker for the System under Alabama law. *See Hunt v. American Bank & Trust Co. of Baton Rouge, La.*, 606 F. Supp. 1348, 1356 (N.D. Ala. 1985), *aff'd*, 783 F. 2d 1011 (11th Cir. 1986 (noting that a receiver "stands in the shoes" of the entity in receivership); *Day v. Farmers' & Merchants' Bank of Hartselle*, 157 So. 439, 443 (Ala. 1934) (same). The Debtor has, therefore, already lost exclusive possession and control of the System by a final, un-appealed order of a state court that vested that possession and control in a duly-appointed officer of the court – the Receiver. Further, under Alabama law, the State Court by rights is the court with jurisdiction over the Receiver and its actions. *Ex Parte Davis*, 162 So. at 308; *Moody v. State ex rel. Payne*, 329 So.2d 73, 78 (Ala. 1976). Section 903 ensures that the Debtor's Chapter 9 filing in no way abrogates the Receiver Order or the State Court's jurisdiction over its duly-appointed Receiver. Because the Receiver's appointment was the result of the valid exercise of the State of Alabama's authority over its political subdivision and because the Receiver is an officer of its appointing State Court, Section 903 prevents the court from disturbing the Receiver Order.

As explained above, since Section 543 is inapplicable to Chapter 9, there is no Bankruptcy Code section requiring the turnover of property and thus no conflicting federal bankruptcy law. In fact, the clear intent behind the omission of Section 543 in Chapter 9 cases was to *prevent* a debtor from overturning valid state action to appoint a custodian over a debtor. Yet, the Debtor would read turnover authority back into Chapter 9 by way of Section 362. In

doing so, the Debtor is relying on this Court to ignore Section 903 and the Tenth Amendment and expand Section 362 to an unconstitutional application. The Court should decline such an invitation. Thus, the Court should find that the Receiver should be allowed to continue to operate and control the System pursuant to the terms of the Receiver Order and under the supervision of the State Court.

3. Under Section 922(d), the Automatic Stay Does Not Apply to the System's Revenues and Deposit Accounts Because they are Special Revenues.

The Court likewise should allow the Receiver to remain in possession of the System in order to apply the System's revenues to the System's debt consistent with Sections 922(d), 927 and 928 of the Bankruptcy Code. The Receiver, under Section 2(d) of the Receiver Order, is provided "sole and exclusive right to receive, collect, take possession of, and preserve all accounts, incomes, profits, and other revenues generated from and by the System, that the Receiver, in its business judgment, may deem necessary for the administration or the operation of the System." In 1988, Congress amended the Bankruptcy Code to address the specific issue of special revenue bonds in Chapter 9 cases by adding Sections 902(2), 922(d), 927 and 928 to the Code. As one court has put it,

> The 1988 Amendments were intended to preserve a dichotomy between general obligation and special revenue bonds for the collective benefit of bondholders (to secure the benefit of their bargain), municipalities (to maintain the effectiveness of the revenue bond financing vehicle) and taxpayers (to ensure that revenue obligations were not transformed into general obligations).

In re Heffernan Memorial Hosp. Dist., 202 B.R. 147, 148 (Bankr. S.D. Cal. 1996); *see also* H.R. Rep. No. 100-1011, at 4, 6-8 (1988), *as reprinted in* 1988 U.S.C.C.A.N. 4115, at 4118. Each of these sections is applicable to the Receiver's present request, and taken together, these Sections require the Court to grant the Receiver's motion.

The System's revenues and deposit accounts are clearly "special revenues" as defined in Section 902(2) of the Code.[5] Section 902(2) provides:

> (2) "special revenues" means—
>
> (A) receipts derived from the ownership, operation, or disposition of projects or systems of the debtor that are primarily used or intended to be used primarily to provide transportation, utility or other services, including the proceeds of borrowings to finance the projects or systems[.]

11 U.S.C. § 902(2)(A). The System's revenues and the money in the System's deposit accounts are receipts derived from the operation of the System, which is a system intended to provide sewer (i.e. utility) services.

Furthermore, the Debtor and the Indenture Trustee intended that the System's revenues and the deposit accounts should be treated as special revenues as evidenced by Section 2.2 of the Indenture, which states that the indebtedness under the Indenture would not be a general obligation of the Debtor, and Section 11.6 of the Indenture, which provides that any surplus in the System's revenues after the Debtor makes the disbursements required in Article 11 of the Indenture can only be used for purposes related to the System. *See Heffernan Memorial Hosp. Dist.*, 202 B.R. at 149 (finding that sales tax revenues were "special revenues" because sales tax was not available for general obligations and bonds were not a debt or liability of the debtor but were payable solely from the sales tax).

These special revenues were pledged to the Trustee as security for the Debtor's indebtedness under the warrants pursuant to Section 2.1 of the Indenture. Section 922(d) exempts "the application of pledged special revenues in a manner consistent with section 927 of this title to payment of indebtedness secured by such revenues" from the automatic stay of

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[5] The Debtor does not dispute this fact in its Demand Letter.

sections 362 and 922(a). 11 U.S.C. § 922(d). Section 928 of the Bankruptcy Code, which governs the post petition effect of a security interest in special revenues, provides that notwithstanding other provisions of the Bankruptcy Code, "special revenues acquired by the Debtor after commencement of the case shall remain subject to any lien resulting from any security agreement entered into by the Debtor before the commencement of the case." Thus, as pledged "special revenues", the automatic stay does not apply to the System's revenues and deposit accounts. Further, as pledged "special revenues", the post-petition revenues of the System remain encumbered by the Trustee's lien under Section 928, with any such lien being subject to the necessary operating expenses of the System (according to Section 2.1 of the Indenture, the Indenture Trustee's lien already is subject to the System's operating expenses).

When dealing with special revenues pledged to pay special revenue bonds, such as the indebtedness issued under the Indenture, the intent of Congress is clear—Congress wanted pledged special revenues to continue to be applied to the debt they secure while a municipality is in bankruptcy. To that end, reading the omission of Section 543 in Section 901(a) together with Sections 922(d), 927, and 928, Congress intended that bankruptcy courts should not interfere with bondholder's rights to payment from special revenues, including where a receiver has been appointed to ensure that the bondholders receive the benefit of their bargain when a debtor (such as this Debtor) is unwilling to comply with its obligations. Section 903 further prevents the Court from any attempt to limit the Receiver's control over the System. Chapter 9 therefore embodies a coherent statutory scheme that requires this Court to enter an order confirming the Receiver's authority over the System. Accordingly, the Court should allow the Receiver to remain in place in order to continue to apply the System's net revenues to the System's debt as contemplated under Sections 922(d), 927, and 928.

B. The Receiver Should Retain Authority Under the Receiver Order To Set Rates for the System

As described in the fact summary, when the State Court appointed the Receiver pursuant to Ala. Code § 6-6-620, it gave the Receiver the exclusive authority to fix and charge rates. *See* Exhibit A, at p. 8, ¶ 2c. The authority to appoint a receiver to subsume a portion of a county's authority is countenanced by Alabama law, particularly where the court finds a failure to perform duties. *Carter v. State ex rel. Bullock County*, 393 So. 2d 1368, 1371 (Ala. 1981) (Court did not err in appointing receiver over county tax assessor where tax assessor's refusal to perform his duties materially hampered legitimate and essential governmental functions of county); *see also* Ala. Code § 11-81-180 (providing for appointment of receiver over systems including sewer system);[6] *Bankhead v. Town of Sulligent*, 155 So. 869 (Ala. 1934) (providing that appointment of a receiver ensures that statutory lien is not "a meaningless expression"). Furthermore, the State Court should have exclusive jurisdiction under Alabama law to determine whether the Debtor may challenge the Receiver's authority. *See Ex parte Davis*, 162 So. 306, 308 (Ala. 1935).

After extensive work cutting costs and providing detailed budgets and capital plans, the Receiver provided notice of its intent to increase the rates charged by the System. These increases are necessary to produce enough revenue to cover costs of operations and service the System's debts, particularly because the Debtor refused to increase rates in any amount from 2008 until the present despite agreeing in the Indenture to maintain rates sufficient to service the System's debt.[7] As explained below, nothing in the Bankruptcy Code or applicable state law

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[6] This code provision specifically governs analogous bond issuances pursuant to Ala. Code § 11-81-160 *et seq.* The warrants secured by the System revenues were issued under a similar chapter, Ala. Code § 11-28-1 *et seq.*

[7] Although the Receiver does not take a position on the validity of the Debtor's filing of the petition, it should be noted that at least one court has found that the refusal to use assessment and taxing powers supported a finding that the filing was in bad faith. See *In re Sullivan County Regional Refuse Disposal District*, 165 B.R. 60 (Bankr. D. N.H. 1994) ("Congress did not intend that a municipality that made no effort to use its assessment or taxing powers

allows the Debtor to curtail the Receiver's rate-making authority at this juncture. Accordingly, the Court should enter an order confirming that the Receiver retains its authority to fix and charge rates for the System.

1. The Arguments Supporting the Right of the Receiver to Retain Control of the System Support the Receiver's Ratemaking Authority

The arguments the Receiver put forth above in Section A above likewise apply to the Receiver's ratemaking authority, and the Receiver incorporates them herein by reference.

2. The Bankruptcy Code Supports the Receiver's Continued Authority to Set Sewer Rates

The Debtor cannot divest the Receiver of authority to set sewer rates for the System under the Bankruptcy Code for three reasons. First, since the Receiver, pursuant to a final, un-appealed State Court Receiver Order, has the sole authority to set rates for System users, the rate-making processes proposed by the Receiver are exempt from the automatic stay. Second, the Debtor cannot propose a plan that would divest the Receiver of all rate-making authority because such a plan would be contrary to state law. Third, the Receiver, as the applicable rate-making authority for the System, in effect is the Debtor for purposes of Section 904; accordingly, the Court does not have the authority to interfere in the Receiver's rate-making processes.

First, it is unclear whether any action by the Receiver to raise rates can be considered an action against the Debtor or the Debtor's property at all; however, even if such action is covered by the stay provisions of Section 362(a), such action would be exempt from the stay according to Section 364(b)(4). This section provides that the filing of a bankruptcy petition does not stay:

> under paragraph (1), (2), (3), or (6) of subsection (a) of this section, of the commencement or continuation of an action or proceeding by a governmental unit

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to meet its obligations before filing nevertheless could come into the bankruptcy courts to resolve what is essentially a contractual dispute with one of its creditors.").

> . . . to enforce such governmental unit's or organization's police and regulatory power[.]

11 U.S.C. § 362(b)(4). Courts have interpreted this section to exempt rate-making actions taken by rate-making bodies from the effects of the automatic stay. *See Louisiana Public Service Commission v. Ralph R. Mabey (In re Cajun Electrical Power Cooperative, Inc.)*, 185 F.3d 446, 457-58 (5th Cir. 1999); *In re Pacific Gas & Elec. Co.*, 263 B.R. 306, 316-20 (Bankr. N.D. Cal. 2001). Thus, actions taken by the Receiver (as the sole rate-making authority for the System) to set rates are exempt from the stay.

Second, now that the County has irretrievably lost the authority to fix and charge sewer rates pursuant to valid State action, it cannot now seek an order from this court or propose a plan to gain that authority back absent an appeal to the court that originally appointed the Receiver (that is, the State Court). This authority is typical of that of a State attempting to control its municipalities for purposes of Section 903. Several bankruptcy courts have decided that a Chapter 9 debtor cannot propose a plan that contravenes state law. *See In re Mount Carbon Metropolitan Dist.*, 242 B.R. 18, 41 (Bankr. D. Colo. 1999) ("A Chapter 9 plan must be consistent with the governmental nature and obligations of the Chapter 9 debtor."); *In re City of Colorado Springs Springcreek Gen. Improv. Dist.*, 177 B.R. 684, 692-93 (Bankr. D. Colo. 1995) (state law requirement of election for issuance of new bonds by Chapter 9 debtor must be complied with for plan to be confirmed); *In re Sanitary & Improv. Dist., # 7*, 98 B.R. 970, 974-75 (Bankr. D. Neb. 1989) (Nebraska court decision required bondholders to be paid in full before payments could be made on warrantholders; debtor's Chapter 9 plan had to comply with this requirement). The Debtor's current position is at odds with Alabama law, which provided for the appointment of the Receiver in the first place pursuant to a final, un-appealed order, and which provides that the State Court, as the court that appointed the Receiver, should be the gatekeeper

of questions regarding the Receiver's authority. Accordingly, the Court should find that the Debtor's bankruptcy filing in no way altered the Receiver's authority over the System.[8]

Third, because the Receiver essentially is the Debtor for purposes of the operation of the System, Section 904 would prevent this Court from directing the Receiver not to raise rates. Ala. Const. amend. 73 granted the County the authority to fix and charge sewer rates for the System. As stated above, the Receiver stands in the shoes of the County for purposes of operating the System and fixing and charging sewer rates. *See Hunt*, 606 F. Supp. at 1356; *Day*, 157 So. at 443.

Under Section 904, bankruptcy courts cannot enter orders or decrees that "interfere with—(1) any of the political or governmental powers of the debtor; or (2) any of the property or revenues of the debtor." 11 U.S.C. § 904(1) and (2). This Court cannot direct the Receiver, which stands in the shoes of the County and is thus the "Debtor" for all intents and purposes related to the System, not to raise rates because doing so would violate the Receiver's authority that it exercises on behalf of the Debtor and the revenues of the System over which the Receiver has exclusive control. *See Hollstein v. Sanitary and Improvement Dist. No. 7 of Lancaster County, Neb. (In re Sanitary and Improvement Dist. No. 7 of Lancaster County, Neb.)*, 96 B.R. 967, 971 (Bankr. D. Neb. 1989) (dismissing adversary proceeding against trustees of board of debtor sewer district because "the trustees are employees, officers or agents of the SID and civil action against them for their official acts can be brought only pursuant to the Nebraska Political Subdivision Tort Claims Act"). Here, if members of the County Commission want to challenge

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[8] Similarly, Section 1129(a)(6), which is incorporated into Chapter 9 by Section 901(a), only allows confirmation of a plan if "[any] governmental regulatory commission with jurisdiction, after confirmation of the plan, over the rates of the debtor has approved any rate change provided for in the plan, or such rate change is expressly conditioned on such approval." 11 U.S.C. § 1129(a)(6). The Receiver, as this rate-making authority, arguably should have the right to consent to any plan proposals.

the Receiver's authority, they must do so in the Receivership Court, since the Receivership Court is the gatekeeper for actions against the Receiver. *See Ex Parte Davis*, 162 So. at 308; *Moody v. State ex rel. Payne*, 329 So.2d 73, 78 (Ala. 1976). This Court cannot interfere with the Receiver, which has stepped into the shoes of the Debtor for purposes of running the System, or with the Receiver's authority to fix and charge the System's rates. Accordingly, the Court should enter an order stating that Section 904 deprives the Court of authority to prevent the Receiver from fixing and charging rates pursuant to its authority under the Receiver Order.

C. The Court Should Abstain from Exercising Jurisdiction Over the System and the Receiver Pursuant to the Rooker-Feldman Doctrine, 28 U.S.C. § 1334, and Federal Law preventing Federal Court Intervention in Rate-Making Processes.

1. The Rooker-Feldman Doctrine Prohibits the Court from Disturbing the Receiver Order.

The Rooker-Feldman doctrine prohibits this Court from disturbing the Receiver Order because any change to the outcome of the State Court proceedings would for all practical purposes be an appeal to a federal court by a state-court loser. As the Eleventh Circuit explained:

> [T]he Rooker-Feldman doctrine recognizes that federal district courts do not have jurisdiction to act as appellate courts and precludes them from reviewing final state court decisions. The Rooker-Feldman doctrine applies only to cases that are brought by state-court losers complaining of injuries caused by state-court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments. The doctrine bars the losing party in state court from seeking what in substance would be appellate review of the state judgment in a United States district court, based on the losing party's claim that the state judgment itself violates the loser's federal rights.

Paletti v. Yellow Jacket Marina, Inc., 395 Fed. Appx. 549, 553 (11th Cir. 2010) (internal citations and quotation marks omitted). The Rooker-Feldman doctrine applies to all federal courts below the United States Supreme Court, including bankruptcy courts. *See, e.g.*, *In re*

Madera, 586 F.3d 228, 232 (3d Cir. 2009) ("[T]his doctrine applies equally to federal bankruptcy courts."); *In re Jenkins*, 258 B.R. 251, 264 (Bankr. N.D. Ala. 2001) ("[I]f the state court has litigated the issue of dischargeability, then the Rooker-Feldman doctrine would preclude a bankruptcy court's review of that judgment and decision.").

The Rooker-Feldman doctrine even extends to protect the final orders of state courts when those orders make determinations directly related to core bankruptcy proceedings. In one bankruptcy case appealed to the Eleventh Circuit, two creditors obtained a judgment against a debtor in state court and recorded liens. *In re Schweizer*, 399 Fed. Appx. 482, 483 (11th Cir. 2010). In a separate state action, the creditors filed an action to foreclose their liens. *Id.* The debtor claimed a homestead exemption under Florida law, and the parties were in dispute as to which portion of the land should be subject to the exemption. *Id.* The state court resolved the dispute in the creditors' favor, and the debtor did not appeal the decision. *Id.*

After the deadline for appeal had passed, the debtor filed a petition for bankruptcy under Chapter 7. *Id.* When the debtor attempted to claim a different portion of the land as his homestead exemption than what the state court had determined – and eliminate the creditors' liens – the creditors objected. *Id.* The bankruptcy court held that it "could not reexamine the state court's determination" due to the Rooker-Feldman doctrine and denied the debtor's motion. *Id.* The Eleventh Circuit affirmed, holding that the state court's un-appealed final judgment, which defined the scope and existence of the debtor's homestead exemption, and thus the scope and existence of the creditors' liens, could not be reexamined by the bankruptcy court. *Id.* at 484; *see also In re Ferren*, 203 F.3d 559, 559-60 (8th Cir. 2000) (holding that a bankruptcy court lacks the jurisdiction to entertain an adversary proceeding that seeks to void a state court

judgment which authorized the foreclosure and sale of real property in satisfaction of a lien because of the Rooker-Feldman doctrine).

Similarly, the Receiver Order defines the scope and existence of the County's property interest in the System. The appointment of a receiver is the key component to enforcing the warrantholders' lien rights, and the determination as to the scope of the Receiver's authority and authority has already been determined by a final judgment of the State Court. Removing the Receiver, or any aspect of the Receiver's authority and control over the System, including the Receiver's authority to fix and charge rates, would have the effect of redefining the scope and existence of the parties' agreed-upon interest in the System. Because such a decision would impermissibly transform this Court into an appellate court reexamining the State Court's decision, Rooker-Feldman is triggered and divests this Court of power and jurisdiction. Any attempt by the Debtor to have the Receiver Order set aside or modified by this Court is merely an attempt to use Chapter 9 as a means to collaterally attack an order entered over a year ago that the Debtor has chosen not to appeal.

Additionally, removing or modifying the Receiver's authority under the Receiver Order would deny the warrantholders rights that were granted by the Indenture and judicially confirmed by the Receiver Order. In a case from New York, a creditor sought relief from the automatic stay in order to foreclose on a secured interest in real property. *In re Agard*, 444 B.R. 231, 235 (Bankr. E.D.N.Y. 2011). The debtor contested the motion for relief by challenging the creditor's standing to foreclose. *Id.* at 242. The debtor argued that Rooker-Feldman should not apply because he was not asking the bankruptcy court to set aside the judgment of foreclosure, but was instead making a jurisdictional challenge. *Id.* at 243. The bankruptcy court rejected this argument because the "net effect of upholding the Debtor's jurisdictional objection in this case

would be to deny [the creditor] rights that were lawfully granted to [the creditor] by the state court," which is "tantamount to reversal." *Id.* at 244.

The Receiver's appointment is a remedy to effectuate the warrantholders' security interest exclusively protected by Sections 922(d), 927 and 928. Removing the Receiver or reducing its authority in any way would be "tantamount to a reversal" of the Receiver Order. Thus, the Rooker Feldman doctrine precludes the Bankruptcy Court from disturbing the final, un-appealed Receiver Order by removing the Receiver or modifying the Receiver's authority.

2. The Court Should Abstain Under 28 U.S.C. § 1334.

a. Mandatory Abstention under 28 U.S.C. § 1334(c)(2) and pursuant to the Johnson Act (28 U.S.C. § 1342) is required in this case.

Mandatory abstention is governed by 28 U.S.C. § 1334(c)(2) which provides that:

> in a proceeding based upon a state law claim or state law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a state forum of appropriate jurisdiction.

28 U.S.C. § 1334(c)(2). The proceedings that resulted in the Receiver Order, and any effort to undo their results, do not involve any federal rights or causes of action. In fact, the federal District Court for the Northern District of Alabama previously abstained from hearing the suit brought by the Indenture Trustee to appoint a receiver in part based upon the Johnson Act (28 U.S.C. § 1342), which strips federal courts of jurisdiction in a proceeding seeking to appoint a receiver with ratemaking authority over a political subdivision. Based upon Section 928's effect on postpetition security interests in special revenues, and because Bankruptcy Code Section 543 does not apply in Chapter 9, there is no claim arising under or arising in a case under title 11

related to the Receiver Order. Therefore, mandatory abstention is appropriate and the Receiver should continue to operate and control the system pursuant to the Receiver Order and under the supervision of the Alabama State Courts.

b. Permissive Abstention under 28 U.S.C. § 1334(c)(1) is appropriate in this case.

Permissive abstention is appropriate in this case and would result in the Receiver continuing to operate and control the System. Courts in the Northern District of Alabama have followed a 12-factor test in determining whether permissive abstention is appropriate. Those factors are:

> 1) the effect of abstention, or lack thereof, on the efficient administration of the bankruptcy estate;
>
> 2) the extent to which state law issues predominate over bankruptcy issues;
>
> 3) the difficulty or unsettled nature of the applicable law;
>
> 4) the presence of a related proceeding commenced in state court or other non-bankruptcy court;
>
> 5) the basis of bankruptcy jurisdiction, if any, other than 28 U.S.C. § 1334;
>
> 6) the degree of relatedness or remoteness of the proceeding to the main bankruptcy case;
>
> 7) the substance rather than form of an asserted "core" proceeding;
>
> 8) the feasibility of severing state law claims from core bankruptcy matters to allow judgments to be entered in state court with enforcement left to the bankruptcy court;
>
> 9) the burden of the bankruptcy court's docket;
>
> 10) the likelihood that the commencement of the proceeding in bankruptcy court involves forum shopping by one of the parties;
>
> 11) the existence of a right to a jury trial; and
>
> 12) the presence in the proceeding of non-debtor parties.

Ventura v. Billie B. Line, Jr. et al. (In re Billie B. Line, Jr.), 2008 WL 1699419 at * 4 (Bankr. N.D. Ala. 2008). "Courts should apply these factors flexibly, for their relevance and importance will vary with the particular circumstances of each case, and no one factor is necessarily

determinative." *Cassidy v. Wyeth–Ayerst Laboratories*, 42 F.Supp.2d 1260, 1263 (M.D. Ala. 1999) (*quoting Matter of Chicago, Milwaukee, St. Paul & Pacific R.R. Co*., 6 F.3d 1184, 1189 (7th Cir.1993)).

Here, the factors weigh heavily in support of the appropriateness of permissive abstention. The District Court for the Northern District of Alabama found that there was evidence of fraud surrounding the construction of the System and the sale of the Warrants, and that the County ignored the advice of its consultants and suppressed information concerning the System's problems. Further, the court found that the County mismanaged the System and did not properly account for the System. The District Court and the Jefferson County Circuit Court further found that the appointment of the Receiver would enhance the operational efficiencies of the System. Since its appointment, the Receiver, who had been nominated by the County as Special Master, has formulated a comprehensive business plan for the first time in the System's history, reduced costs, improved billing and collection practices, and drafted a capital improvement plan. Under the circumstances, the continued operation of the System by the Receiver would enhance, rather than adversely impact the administration of the County's Chapter 9 case.

Moreover, additional factors support the Court's abstention, including that:

(a) The System is segregated from other creditors of the County and all revenues of the System will continue to make payments to the Indenture Trustee under the Indenture;

(b) Continued operation of the System by the Receiver will not impact the County's other non-System related creditors.

(c) The issues related to the Receiver's operation and control of the System are entirely based upon state law causes of action and do not implicate federal bankruptcy law directly. In

fact, no federal court can have jurisdiction over the ratemaking authority of the Receiver under the Receiver Order;

(d) Section 928 of the Bankruptcy Code provides that the special revenues remain subject to the Warrantholder's lien postpetition, and Section 922(d) provides that the automatic stay does not apply to application of those revenues to the outstanding Warrants;

(e) The State Court is already intimately familiar with the complexities of the System and the Receiver, and the State Court has continued to supervise any and all disputes concerning the Receiver Order, and has continued to monitor the case closely to ensure the Receiver's operation is consistent with the law.

Therefore, because the receivership is solely a matter of state law and abstention will enhance the Court's ability to administer the Chapter 9 case, the Court should abstain from involvement in matters related to the Receiver and the Receiver Order, thus leaving the Receiver in place to operate and control the System and administer the System and its revenues, including by fixing and charging rates, pursuant to the Receiver Order and the oversight of the State Court.

3. This Court Likewise Does Not Have Jurisdiction Over or Should Abstain from Any Decision Impacting Sewer Rates

The Court does not have specific authority to curtail the Receiver's ratemaking authority, whether by injunction or through confirming a non-consensual plan of adjustment. In fact, both Congress and the federal courts have articulated a consistent policy of non-interference with State processes for setting intrastate utility rates.

The Supreme Court has long held that "the regulation of utilities is one of the most important of the functions traditionally associated with the police power of the States." *Arkansas Electric Cooperative Corp. v. Arkansas Public Serv. Comm'n*, 461 U.S. 375, 377 (1983); *accord Pacific Gas & Electric Co. v. State Energy Resources Conservation & Development Comm'n*,

461 U.S. 190, 205-206 (1983); *Cent. Hudson Gas & Elec. Corp. v. Public Serv. Comm'n of New York*, 447 U.S. 557, 569 (1980). To that end, "the power to regulate intrastate services such as utilities has historically been reserved to the states by Congress pursuant to the provisions of the tenth amendment of the United States Constitution." *Gulf Water Benefaction Company v. The Public Utility Commission of Texas*, 674 F. 2d 462, 467 (5th Cir. 1982) (citing *Public Utilities Commission for State of Kansas v. Landon*, 249 U.S. 236 (1919)).

Therefore, as *Gulf Water* articulates, "As a general rule, federal courts should not intervene in the state rate-making process unless the remedy in state court is inadequate." *Gulf Water*, 674 F. 2d at 467 (citing *Tennyson v. Gas Service Co.*, 506 F. 2d 1135, 1141 (10th Cir. 1974)). In affirming the bankruptcy court's dismissal of an adversary proceeding in which the debtor sought to challenge a rate-making agency's rate-making process, *Gulf Water* stated that

> the bankruptcy court, when confronted with a state statute, a state regulatory agency and a highly technical matter involving a specialized area of state procedure (utility regulation), determined that the state court would be the better forum to resolve this utility rate controversy. . . . The Court finds, as did the bankruptcy court, that state procedural remedies are available to the debtor-appellant.

Gulf Water, 674 F. 2d at 467. This Court likewise lacks the authority to enjoin the Receiver from exercising its rate authority under Section 105, despite the Debtor's assertion that the Receiver's authority undermines the Debtor's ability to propose a plan of adjustment. *See In re Cajun Electric Power Cooperative, Inc.*, 185 F. 3d 446, 452-53, 458 (5th Cir. 1999) (reversing entry of injunction by the bankruptcy court prohibiting reduction in debtor-utility's rates as an abuse of discretion). Additionally, the Bankruptcy Code itself attempts to leave in place state rate-making structures. *See* 11 U.S.C. §§ 362(b)(4); 1129(a)(6).

Further, *Gulf Water* also determined that the Johnson Act, a congressional control over federal court interference in rate-making procedures, likewise prevented the bankruptcy court

from determining issues related to state rate-making procedures. *Id.* at 467-68. The Johnson Act provides:

> The district courts shall not enjoin, suspend or restrain the operation of, or compliance with, any order affecting rates chargeable by a public utility and made by a State administrative agency or a rate-making body of a State political subdivision, where:
>
> (1) Jurisdiction is based solely on diversity of citizenship or repugnance of the order to the Federal Constitution; and,
>
> (2) The order does not interfere with interstate commerce; and
>
> (3) The order has been made after reasonable notice and hearing; and,
>
> (4) A plain, speedy and efficient remedy may be had in courts of such State.

11 U.S.C. § 1342. The clear intent of the Johnson Act is to channel normal rate litigation into the state courts; and federal judicial review is particularly inappropriate where state proceedings are pending or have been completed. *See Brideport Hydraulic Co. v. Council on Water Co. Lands of State of Conn.*, 453 F. Supp. 942, 954 (D. Conn. 1977), *aff'd*., 439 U.S. 999 (1978); *City of Meridian, Miss. v. Mississippi Valley Gas Co*., 214 F.2d 525, 526 (5th Cir. 1954).

As explained above, Judge Proctor previously determined that he did not have authority to appoint a receiver over the System because of the Johnson Act. The parties then fully litigated the issue of the Receiver's authority to fix and charge rates in the State Court, after which the State Court granted a summary judgment motion and entered a final order appointing the Receiver, investing the Receiver with the authority to fix and charge rates, and divesting the Debtor of this authority. The Receiver Order therefore made the Receiver the "rate-making body" responsible for fixing and charging rates in Jefferson County. Further, the Receiver, as explained in the Interim Report, will only authorize rate increases after notice and hearing. The Debtor cannot now ask the Court to reinvest it with authority over rate-making procedures.

Doing so would violate the Tenth Amendment principals articulated in *Gulf Water* as well as the Johnson Act.

The Receiver Order, a final order that the Debtor failed to appeal, specifically granted the Receiver, to the exclusion of any other person – including the Debtor – the sole authority to fix and charge sewer rates. As already stated above, the Rooker-Feldman doctrine prevents this Court from in effect reviewing and overturning the State Court's determination that the Receiver should be the entity setting sewer rates. The Debtor litigated this issue and lost. It cannot now ask this Court to re-determine this issue and nullify an express power of the Receiver – if the Debtor wanted this type of relief it should have appealed the Receiver Order before the time for appeal expired a year ago.

The Debtor's attempt to remove the Receiver or negate the Receiver's rate-making authority is nothing more than a negotiating tactic meant to harm the System's creditors. As explained fully above, the System's revenues, as special revenues under the Bankruptcy Code, continue to secure the indebtedness evidenced by the warrants post-petition and must continue to be applied to that indebtedness and cannot be used to pay other creditors of the Debtor per Sections 922(d) and 928. Further, the warrantholders have no recourse to the general revenues of the Debtor per Section 927 – they can only look to the System's revenues for payment. Consequently, the System's creditors have everything to lose in the event rate-making authority is returned to the Debtor. By contrast, retaining the Receiver, which is in a better position to act in a disinterested manner in the best interests of all parties, will benefit creditors of the System without in any way affecting the Debtor or the Debtor's other creditors since all of the System's revenues must be applied to pay the System's operating expenses and pay the System's creditors.

For all of these reasons, the Debtor simply cannot seek an order of this Court that in any way divests the Receiver of its authority, including the authority to fix and charge rates. Accordingly, the Receiver is entitled to an order confirming its rate-making authority.

D. Even if the Court Declines To Abstain and Finds That the Automatic Stay Does Apply to the System or the System Revenues, Cause Exists for Relief from the Stay to Allow the Receiver to Continue to Operate the System.

Section 362(d)(1) of the Bankruptcy Code states that the Court may terminate the automatic stay contained in Section 362(a) "for cause, including the lack of adequate protection of an interest in property of such party." 11 U.S.C. §362(d); *In re Indian River Estates, Inc.*, 293 B.R. 429, 432-33 (Bankr. N.D. Ohio 2003); *In re Bushee*, 319 B.R. 542, 551 (Bankr. E.D. Tenn. 2004). As used in Section 362(d)(1), "cause" is a "broad and flexible concept which permits a bankruptcy court, as a court of equity, to respond to inherently fact-sensitive situations." *Indian River*, 293 B.R. at 433; *In re Texas State Optical, Inc.*, 188 B.R. 552, 556 (Bankr. E.D. Tex. 1995).

Here, cause exists for relief from the automatic stay because the Debtor cannot effectively and economically manage the System; however, the Receiver can.

Mismanagement of collateral creating a substantial risk of diminishment in the collateral's value is grounds for relief from stay. *In re New Era Co.*, 125 B.R. 725, 730 (S.D.N.Y. 1991); *see also In re Asheville Bldg. Assocs.*, 93 B.R. 913, 917 (Bankr. W.D.N.C. 1988) (relief from stay was justified where receiver had been appointed pre-petition due to debtor's mismanagement of property). Moreover, decrease in value of the collateral has long been recognized as grounds for relief from stay due to lack of adequate protection. *See, e.g.*, *In re Mosello*, 195 B.R. 277 (Bankr. S.D.N.Y. 1996); *In re Bleecker Street Assocs.*, 156 B.R. 405 (Bankr. S.D.N.Y. 1993).

Here, the State Court premised the Receiver's appointment on the defaults and evidence of mismanagement of the System by the Debtor. In fact, the State Court found that without a receiver operating the System, the Debtor's continued possession and management of the System "will reduce the overall value of the Trustee's collateral and result in further irreparable harm to the Trustee and the Parity Security Holders." *See* Exhibit A, at p. 6, ¶ 19. The State Court's findings are rife with examples of the Debtor's mismanagement, including failure to keep books and records for the System and provide the same to the Trustee, absence of planning for maintenance, capital expenditures, and an overall business plan, and lack of political fortitude to raise revenue to properly fund the System. If the System is turned over to the Debtor, these same issues will reassert themselves with resulting "irreparable harm" (in the words of the State Court) to the System's creditors. The Court should avoid such a situation at the outset of this case by allowing the Receiver to remain in place. The Debtor's mismanagement of the System, which has resulted and, if the Receiver is replaced, will continue to result in diminishment of the Trustee's collateral, represents cause for relief from the automatic stay.

Under normal circumstances, Chapter 9 debtors are given significant freedom to operate without the restrictions that apply to a Chapter 11 debtor. But Chapter 11 envisions a procedure where Section 543 can be used to displace a receiver and, if necessary, replace such receiver under Section 1104 with a trustee. As previously noted, 11 U.S.C. § 901 sets forth a list of specific provisions of the Bankruptcy Code applicable in a Chapter 9 proceeding – and absent from that list is 11 U.S.C. § 1104, which provides for the appointment of a trustee with broad powers.[9] It is logical that, since no trustee with broad powers can be appointed in Chapter 9,

[9] There is a narrow exception, contained in Sections 902(5) and 926(a), allowing for appointment of a trustee to pursue an action under one of the debtor's avoiding powers, if the debtor refuses to do so. Outside of this narrow exception, the basic premise of Chapter 9 is that appointment of a trustee is not an alternative available to provide

there should be no ability to remove a receiver who has been put in place prior to bankruptcy due to clear evidence of fraud, mismanagement and misconduct. That is exactly the result that arises out of the structure of Chapter 9 since Section 901 does not include the Section 543 turnover provision. Otherwise, a debtor-municipality whose fraud, mismanagement or misconduct resulted in appointment of a receiver prepetition over a utility or other particular function could simply reverse the result by filing Chapter 9 – knowing that a trustee would not be appointed in the receiver's place. This flawed result only comes if the Court were to effectively allow a turnover of property from the Receiver or strip the Receiver of authority – despite the fact that Section 543 is inapplicable – while no substitute remedy in the form of a trustee is available.

In this case, the Receiver was appointed based upon specific evidence of mismanagement and fraud. Resort to a bankruptcy court order removing a judicially-appointed receiver would allow a municipality to simply "undo" a state's action to control its municipality and at the same time avoid any ongoing monitoring or oversight. To allow the Debtor to circumvent the oversight of the Receiver simply by filing a petition under Chapter 9 would set a perilous precedent for an abuse of the protections of Chapter 9 in future cases.

Finally, the Receiver's possession of the System itself is sufficient to establish cause. *See In re Milford Common J.V. Trust*, 117 B.R. 15 (Bankr. D. Mass. 1990) (mortgagee who had made valid entry pursuant to assignment of rents prior to bankruptcy filing was entitled to relief from stay).

V. Conclusion

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oversight of a debtor's case or operations. Accordingly, a trustee is not an option in Chapter 9 even where fraud, mismanagement and other misconduct is present.

WHEREFORE, PREMISES CONSIDERED, the Receiver requests the Court pursuant to 11 U.S.C. §§ 362(d), 903, 922(b) and (d), and 928 for a determination that the Receiver may continue operating the System and is not required to turn over control of the System, or alternatively, for relief from the automatic stay such as terminating, annulling, modifying or otherwise conditioning the stay, so that the Receiver may continue in possession of, and take any and all action necessary to preserve, protect, administer and operate, the System and collect and pay the revenues from the System, less operating expenses, to the creditors whose claims are secured by such revenues pursuant to the order appointing the Receiver. The Receiver further requests such other, different or additional relief to which it may be entitled.

Respectfully Submitted,

/s/ Timothy M. Lupinacci
Timothy M. Lupinacci
W. Patton Hahn
Max A. Moseley
Daniel J. Ferretti

Attorneys for John S. Young, Jr., LLC, in its capacity as Receiver for the Jefferson County Sewer System

OF COUNSEL:
BAKER, DONELSON, BEARMAN,
CALDWELL & BERKOWITZ, P.C.
420 North 20th Street
1600 Wells Fargo Tower
Birmingham, AL 35203
Tel: (205) 328.0480
Fax: (205) 488.3738

CERTIFICATE OF SERVICE

I hereby certify that a copy of the above and foregoing paper has been served upon the following electronically, or by placing a copy of same in the U.S. Mail, first-class postage prepaid and properly addressed to the following on November 10, 2011:

MASTER SERVICE LIST

VIA E-MAIL	
Jefferson County, Alabama c/o Patrick Darby c/o Jay Bender Bradley Arant Boult Cummings LLP 1819 Fifth Avenue North Birmingham, AL 35203 pdarby@babc.com jbender@babc.com	Jefferson County Special Counsel J.F. "Foster" Clark, Esq. Balch & Bingham, LLC 1901 6th Avenue North 2600 AmSouth Harbert Plaza Birmingham, AL 35203-4644 fclark@balch.com
Jefferson County, Alabama c/o Kenneth Klee c/o Lee Bogdanoff Klee, Tuchin, Bogdanoff & Stern, LLP 1999 Avenue of the Stars, Thirty-Ninth Floor Los Angeles, CA 90067-5061 kklee@ktbslaw.com lbogdanoff@ktbslaw.com	Jefferson County Special Counsel J. Hobson Presley, Jr. Presley Burton & Collier, LLC 2801 Highway 280 South, Suite 700 Birmingham, AL 35223-2483 hpresley@presleyllc.com
Jefferson County Attorney Jeffrey M. Sewell, County Attorney Room 280, Jefferson County Courthouse 716 North Richard Arrington Jr. Blvd. Birmingham, AL 35203 sewellj@jccal.org	Bankruptcy Administrator for the Northern District of Alabama (Birmingham) Office of the Bankruptcy Administrator c/o J. Thomas Corbett, Esq. United States Bankruptcy Court Robert S. Vance Federal Building 1800 5th Ave. North Birmingham AL 35203 Thomas_Corbett@alnaba.uscourts.gov
The Bank of New York Trust Company of Florida, N.A., as Indenture Trustee c/o Gerald F. Mace Waller Lansden Dortch & Davis, LLP 511 Union Street, Suite 2700 Nashville, TN 37219 gerald.mace@wallerlaw.com	The Bank of New York Trust Company of Florida, N.A., as Indenture Trustee c/o Larry Childs, Esq. Waller Lansden Dortch & Davis, LLP Regions Harbert Plaza 1901 Sixth Avenue North, Suite 1400 Birmingham, AL 35203 larry.childs@wallerlaw.com

U.S. Bank, National Association, as Paying Agent 2204 Lakeshore Drive Suite 302 Mail Code: EX-AL-WWPH Homewood, AL 35209 felicia.cannon@usbank.com	JPMorgan Chase Bank, as Liquidity Agent c/o John A. Henry, Jr. Kutak Rock LLP 1801 California Street, Suite 3100 Denver, CO 80202 john.henry@kutakrock.com
Bank of America, N.A. c/o David L. Eades Moore & Van Allen, PLLC 100 North Tryon Street, Suite 4700 Charlotte, NC 28202-4003 davideades@mvalaw.com	The Bank of New York Mellon c/o Thomas C. Mitchell Orrick, Herrington & Sutcliffe LLP The Orrick Building 405 Howard Street San Francisco, CA 94105-2669 tcmitchell@orrick.com
State Street Bank and Trust Company c/o William W. Kannel Mintz, Levin, Cohn, Ferris, Glovsky and Popeo, P.C. One Financial Center Boston, MA 02111 wkannel@mintz.com	The Bank of Nova Scotia c/o James E. Spiotto Chapman & Cutler LLP 111 West Monroe Street Chicago, IL 60603-4080 spiotto@chapman.com
Lloyds TSB Bank PLC c/o James E. Spiotto Chapman & Cutler LLP 111 West Monroe Street Chicago, IL 60603-4080 spiotto@chapman.com	JPMorgan Chase Bank Steve M. Fuhrman, Esq. Simpson Thacher & Bartlett LLP 425 Lexington Avenue New York, NY 10017 sfuhrman@stblaw.com
Societe Generale c/o Mark J. Fiekers c/o Joyce T. Gorman Ashurst LLP 1725 I Street NW, Suite 300 Washington, DC 20006 mark.fiekers@ashurst.com joyce.gorman@ashurst.com	Regions Bank c/o Jayna Partain Lamar Maynard Cooper & Gale, P.C. AmSouth/Harbert Plaza, Suite 2400 1901 6th Avenue North Birmingham, AL 35203-2618 jlamar@maynardcooper.com
Financial Security Assurance c/o Mark N. Berman Nixon Peabody LLP 100 Summer Street Boston, MA 02110-2131 mberman@nixonpeabody.com	Financial Guaranty Insurance Company c/o H. Slayton "Slate" Dabney, Jr. King & Spaulding 1185 Avenue of the Americas New York, NY 10036-4003 sdabney@kslaw.com

Syncora Guarantee, Inc. c/o Quinn Emanuel Urquhart & Sullivan, LLP Jonathan E. Pickhardt Jake M. Shields Jeffrey C. Berman 51 Madison Avenue, 22nd Floor New York, NY 10010 jonpickhardt@quinnemanuel.com jakeshields@quinnemanuel.com jeffreyberman@quinnemanuel.com	Receiver for County's Sewer System John S. Young, Jr. LLC, as Receiver c/o Baker, Donelson, Bearman, Caldwell& Berkowitz, P.C. Timothy M. Lupinacci, Esq. W. Patton Hahn, Esq. 1600 Wachovia Tower Birmingham, AL 35203 tlupinacci@bakerdonelson.com phahn@bakerdonelson.com
National Public Finance Guarantee c/o Adam Bergonzi Chief Risk Officer 113 King Street Armonk, NY 10504 adam.bergonzi@nationalpfg.com	
VIA OVERNIGHT CARRIER	
Cooper Shattuck, Esq. Legal Advisor Office of the Governor State of Alabama Office of the Governor State Capitol, Room N-104 600 Dexter Avenue Montgomery, AL 36130	David Perry, Esq. Finance Director Office of the Governor State of Alabama Office of the Governor State Capitol, Room N-104 600 Dexter Avenue Montgomery, AL 36130
Luther Strange, Esq. Attorney General State of Alabama 501 Washington Avenue Montgomery, AL 36130	Alabama Department of Environmental Management c/o Tom Johnston, Esq. General Counsel P. O. Box 301463 Montgomery AL 36130-1463
Environmental Protection Agency Ariel Rios Building 1200 Pennsylvania Avenue, N.W. Washington, DC 20460	Environmental Protection Agency Atlanta Federal Center 61 Forsyth Street, SW Atlanta, GA 30303-3104
The Securities and Exchange Commission SEC Headquarters 100 F Street, NE Washington, DC 20549	Internal Revenue Service Centralized Insolvency Operation Post Office Box 21126 Philadelphia, PA 19114-0326

JPMorgan Chase Bank Attn: Michael Mak 60 Wall Street New York, NY 10260	Bayerische Landesbank 560 Lexington Avenue 18th Floor New York, NY 10022 Attn: Francis X. Doyle Second Vice President
The Depository Trust Company, on behalf of the holders of the Jefferson County, Alabama, General Obligation Capital Improvement Warrants, Series 2003-A and 2004-A 55 Water Street New York, NY 10041	JPMorgan Chase Bank 60 Wall Street New York, NY 10260 Attn: William A. Austin
Shoe Station, Inc. Attn: Michael T. Cronin, Esq. Johnson Pope Bokor Ruppel & Burns, LLP 911 Chestnut Street Clearwater, FL 33576	U.S. Bank, National Association (as successor to SouthTrust Bank), as paying agent Attn: Felicia Cannon 2204 Lakeshore Drive Suite 302 Mail Code: EX-AL-WWPH Homewood AL 35209
The Bank of New York Mellon Trust Company, N.A. (f/k/a The Bank of New York Trust Company of Florida, N.A.), as registrar, transfer agent and paying agent Attn: Charles S. Northen, IV 505 N. 20th Street Suite 950 Birmingham, AL 35203	National Public Finance Guarantee Corp. (f/k/a MBIA Insurance Corp.), as insurer of the General Obligation Capital Improvement and Refunding Warrants, 2003-A and Series 2004-A Attn: Daniel McManus, General Counsel 113 King Street Armonk, NY 10504
Morris & Dickson Co LLC P.O. Box 51367 Shreveport, LA 71135-1367	City of Hoover P.O. Box 360628 Hoover, AL 35236-0628
University of Alabama Health Services Foundation, P.C. P.O. Box 55309 Birmingham, AL 35255-5309	Beckman Coulter Dept. CH10164 Palatine, IL 60055-0164
AMT Medical Staffing, Inc. P.O. Box 12105 Birmingham, AL 35202	Teklinks Inc. 201 Summit Parkway Homewood, AL 35209
UAB Health System 619 19th Street South Jefferson Tower, Room J306 Birmingham, AL 35249-6805	AMSOL P.O. Box 6633 High Point, NC 27262

AMCAD 15867 North Mountain Road Broadway, VA 22815	Augmentation, Inc. 3415 Independence Drive, Suite 101 Birmingham, AL 35209-8315
John Plott Company Inc. 2804 Rice Mine Road NE Tuscaloosa, AL 35406	Brice Building Co., LLC 201 Sunbelt Parkway Birmingham, AL 35211
Universal Hospital Services P.O. Box 86 Minneapolis, MN 55486-0940	Laboratory Corporation of America P.O. Box 12140 Burlington, NC 27216-2140
Medical Data Systems Inc. 2001 9th Avenue Suite 312 Vero Beach, FL 32963	

/s/ Timothy M. Lupinacci
Of Counsel